



James P. Hallan, President and CEO
Michigan Retailers Association
Senate Economic Development Committee Testimony
January 29, 2014

Mr. Chairman and Committee members, thank you for scheduling this hearing on SB 658 & 659, the Michigan Main Street Fairness Act. My name is Jim Hallan, and I'm president and CEO of the Michigan Retailers Association, which represents more than 15,000 storefronts and e-commerce websites in Michigan. Our members include Main Street jewelers, shoe stores, gift stores, furniture stores, grocery stores and the largest retail chain drug and general merchandise stores operating throughout the country.

This legislation has the broadest possible support among both large and small retailers and is critical to maintaining the business fabric of our communities. Retail is responsible for more than 850,000 jobs in Michigan. One out of every four Michigan jobs is connected to retail. These bills affect every Michigan retail job, because retailers hire employees based on sales. And, unfortunately, our current sales tax law encourages consumers to purchase goods over the Internet from companies outside of Michigan.

The latest figures from the Department of Treasury show that retail businesses in Michigan will lose \$8.5 billion in Michigan-based sales in FY2015 to companies outside Michigan that don't invest in our state, don't employ Michigan workers, don't pay taxes in Michigan and don't collect sales tax on the goods they sell to Michigan residents. That is a lot of encouragement for non-Michigan businesses and a lot of discouragement for our Michigan retailers.

The issue before you today is straightforward.

If you are a retailer with nexus in Michigan, you are required to collect and remit sales tax at the point of sale. In 1992, the U.S. Supreme Court defined nexus as a physical test, so only retailers with a physical presence must currently collect and remit the sales tax.

However, many out-of-state Internet retailers without a strict "physical presence" in the state do operate in the state and sell goods to Michigan consumers. Because the sales tax is not collected by the seller for those sales, the consumer is required to remit the 6% tax as a use tax when he or she files the Michigan personal income tax return. Of course, this system of voluntary compliance is problematic and sets up a situation where people don't know or conveniently forget to remit the use tax when they file their income tax return. The Michigan Department of Treasury found that only 1.5% of the estimated tax liability on remote sales was collected in 2012.

It's also important to note that in 1992 the Internet had not yet been introduced to the public. We are asking you to pass legislation that catches up with technology by redefining nexus based on common business and economic practices that exist today.

(over)

Let's talk about what the bills do, what they don't do and why they are needed.

What does the proposed legislation do?

1. It creates fairness among all retailers by leveling the playing field at the time a sale is made. Every retailer that meets the newly defined nexus test would have to collect sales tax at the point of sale. The 6% pricing advantage that out-of-state Internet retailers currently enjoy at the critical point of time when a sale is made would go away.
2. It creates a new and stronger definition of nexus and recognizes that many out-of-state Internet companies are already operating in Michigan through a vast network of affiliates or subsidiaries. Affiliates are basically an in-state sales force that is paid commissions by the Internet retailer.
3. The bills capture revenue that is currently lost to the state. Treasury estimates Michigan will lose \$508 million in FY 2015 alone by failing to collect sales tax at the time of the sale. Treasury's estimates of the annual loss have climbed every year from the \$326 million figure in 2008.
4. Results from the just-completed holiday shopping season underscore the fact the problem is rapidly growing worse in our state. Amazon posted its best holiday season ever and analysts said total online sales rose more than 10% nationally, compared to between 2% and 3% for in-store sales. That was nationally. In Michigan, the average Michigan Retailers Association store reported only a 0.1% gain over last year.
5. The legislation, by leveling the playing field, would provide additional money to the schools and local government. 73% of the sales tax goes to schools.
6. The bills also make it easier for consumers to pay sales tax at the point of sale rather than reconcile their Internet receipts when they do their personal income tax return. The legislation protects them from added tax payments and penalties in the event of an audit.

What **doesn't** the legislation do?

1. First, it does **not** create a new tax. Remember, if a consumer purchases a product over the Internet and sales tax is not collected at the point of sale, the consumer is required to declare that purchase and pay a 6% use tax when he or she files the personal income tax return.
2. The bills do **not** require Michigan companies to collect sales tax for online sales in other states unless they have established nexus in the state where the goods are sold and that state has a similar law.
3. It does **not** create a collection hardship. It's not the small affiliate but the large company behind the affiliate that is collecting the tax. More important, calculating sales tax is now an automated process. There are several certified service providers recommended by the Streamlined Sales Tax Governing board. And software has even been available on the Amazon website itself.
4. It will **not** create a situation where affiliates will lose their source of income. Almost every major retailer has an affiliate program. There is a home for everyone. Also, in other states where affiliates have been terminated by Internet-only retailers like Amazon and Overstock, the companies have often reinstated those agreements.

(more)

Are the bills constitutional?

Yes. On December 2, the U.S. Supreme Court declined to hear Amazon's and Overstock's appeal on New York's Main Street Fairness law. The state of New York was the first state to pass a Main Street Fairness bill. New York's highest court recently held that its state's Main Street Fairness law is constitutional. Specifically, the court held that the affiliate programs of Amazon and Overstock created sufficient nexus for sales tax collection. SB 658 and 659 are patterned after the New York act.

Shouldn't we wait for Congress to Act?

No. While it is good for Congress to focus on a federal solution, it is only doing so because of actions by the states. 24 states have passed legislation to end the unfair advantage out-of-state online retailers have over in-state retailers. These states include California, Georgia, Illinois, New York and Texas. Amazon now collects in 19 states, and more than 60% of the U.S. population now lives in a state where Amazon collects sales tax.

Moving this legislation forward in Michigan will be another strong message to Congress. And Michigan simply can't wait for another Christmas to go by without some relief. We need to be in control of our destiny and not wait for the gridlock in D.C. to resolve itself.

Quite simply, we should not be giving favored treatment to out-of-state online companies that don't invest in our state. The playing field should be level for all. The thousands of retailers who have invested in Michigan are not looking for favored treatment. Rather, they just want the ability to compete fairly.

This legislation is truly about leveling the playing field between retailers. Brick-and-mortar retailers know all about competition, but they can't compete on the total price of an item when they're put at a 6% disadvantage out of the gate.

Thank you.

#



Frequently asked questions about Main Street Fairness

What is Main Street Fairness legislation and what would it do?

What is Main Street Fairness?

Main Street Fairness is legislation designed to ensure a fair and level field of competition for Michigan's retailers by requiring certain out-of-state online retailers to collect and remit Michigan's sales tax.

How does the legislation work?

The legislation creates a new definition of "physical presence" to include companies, such as Amazon, that operate in Michigan through subsidiaries, affiliate networks or other persons that have substantial nexus with the state.

Does Main Street Fairness only apply to Amazon?

No. The legislation would apply to any out-of-state online or catalog company that has a defined physical presence in Michigan.

What is happening in Michigan under current law?

Who is currently required to collect and remit sales tax?

Only retailers that have a physical presence in Michigan are required to collect and remit the sales tax. Some online companies exploit this loophole and avoid collecting sales tax on goods sold to Michigan residents by doing business in the state through subsidiaries or through a network of affiliates.

Do Amazon and Overstock currently collect Michigan sales tax?

No. But they should! Amazon has a wholly owned subsidiary, Brilliance Audio, located in Grand Haven, Michigan. Additionally, both Amazon and Overstock use a vast network of affiliates in Michigan to sell products through their online sites. Amazon also leases space in downtown Detroit for employees, and *Crain's Detroit Business* reported that the company was expanding its footprint downtown in July 2013.

Aren't online shoppers already required to calculate and pay use tax on their purchases when they file their income tax returns?

Yes, but most do not. The majority of Michigan residents apparently do not know they are required to pay use tax on items purchased from out-of-state online or mail-order companies. This tax is due when an individual files a personal income tax return. In fact, the Michigan Department of Treasury found that only 1.5 percent of the estimated tax liability on remote sales was collected in 2012.¹

How does Main Street Fairness impact Michigan retailers and customers?

Why is Main Street Fairness important to retailers?

Main Street Fairness levels the playing field for Michigan retailers who are at a disadvantage because they are required to collect the 6% sales tax. Without Main Street Fairness, consumers will continue to use brick-and-mortar retailers as showrooms and avoid paying sales tax by purchasing products online from out-of-state companies.

Would all online-only retailers be required to collect and remit sales tax?

No. Only retailers that have a defined physical presence in the state would be required to collect and remit sales tax. The defined physical presence includes companies that operate in Michigan through subsidiaries, affiliate networks or other persons that have a substantial nexus with the state.

¹ Michigan Department of Treasury, "Michigan Sales and Use Taxes 2012," August 2013. Available: http://www.michigan.gov/documents/treasury/SalesUseTaxReport2012_432538_7.pdf.

If I have a brick-and-mortar store located in Michigan, how would the legislation affect me?

Because you already have a physical presence in Michigan, you are already required to collect and remit Michigan sales tax. The legislation would remove the competitive advantage out-of-state online companies have and would enable you to compete on a level playing field.

If I have a brick-and-mortar store in Michigan but I sell products online to other states, would the legislation require me to collect and remit sales tax for other states?

No. The legislation only deals with Michigan sales tax on items sold in Michigan. Some other states have passed similar legislation; however, you would not be required to collect and remit sales tax in any of those states unless you have a physical presence in that state.

As a consumer, what are my tax obligations for online or catalog purchases?

Under current law, consumers are charged a 6 percent sales tax at the point of sale if the retailer has a physical presence in Michigan. A 6 percent use tax is owed on purchases where sales tax is not charged at the point of sale. The use tax must be calculated and reported on an individual's state income taxes. Main Street Fairness legislation would simplify the collection process for consumers.

Why should we act now?

What impact does the legislation have on the state?

The Michigan Department of Treasury estimates that \$508 million will be lost in FY 2015 due to uncollected sales tax revenue – largely from remote purchases – and the Department projects that number to increase each year.² Put another way, that means Michigan retail businesses will lose \$8.5 billion in sales (and the jobs that flow from those sales) to companies outside Michigan that don't invest in our state, don't employ Michigan workers and don't pay taxes in Michigan. That is a dagger in Michigan's economy and our local communities. Schools and local governments receive the majority of sales tax dollars raised, with 73 percent going to the school aid fund and 24 percent going to local governments.

Is it constitutional?

Yes. On December 2, 2013 – “Cyber Monday” – the U.S. Supreme Court *declined* to hear Overstock's and Amazon's appeal on New York's Main Street Fairness legislation. Earlier this year, the New York Court of Appeals, the State's highest court, held that New York's Main Street Fairness law was *constitutional*. Specifically, the New York Court of Appeals held that the affiliate programs of Amazon and Overstock created sufficient nexus for sales tax collection.

What are other states doing to address this problem?

24 states³ have passed legislation to end the unfair advantage out-of-state online retailers have over in-state retailers. These states include California, Georgia, Illinois, New York and Texas. And Amazon now collects sales tax in 19 states⁴, an action that was often prompted by legislation.⁵ More than 60% of the United States population now lives in a state where Amazon collects sales tax.

I've heard a federal solution is the only way to really change the law, is this true?

No. While Congress is the only entity that can tax interstate commerce, states can levy and address how state-based taxes are collected. While it is good for Congress to focus on a federal solution, it is only doing so because of the actions by the states.

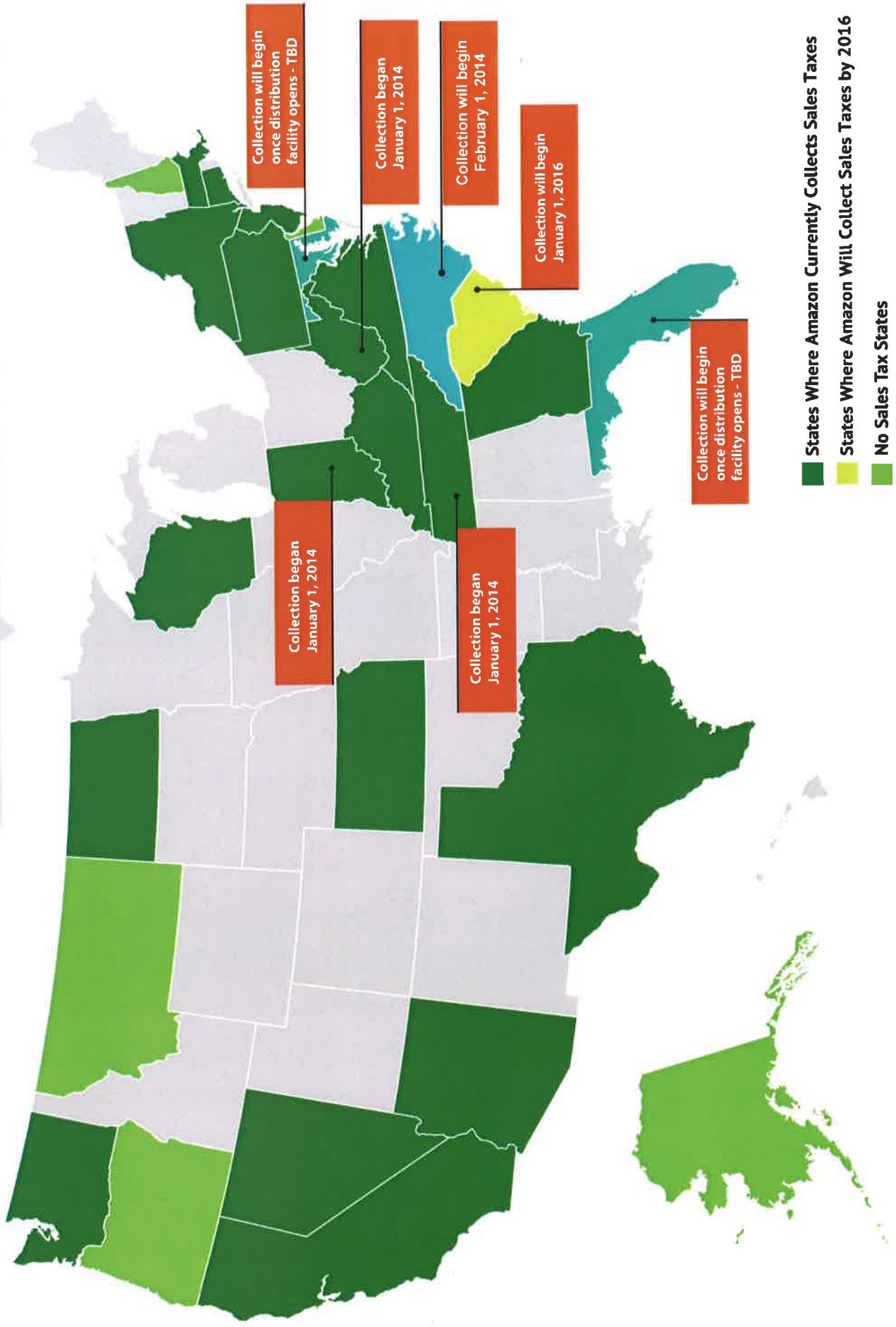
² Michigan Department of Treasury, “Michigan Sales and Use Taxes 2012,” August 2013. Available: http://www.michigan.gov/documents/treasury/SalesUseTaxReport2012_432538_7.pdf.

³ The 24 states that have passed legislation are: AR, CA, CO, CT, GA, IA, IL, KS, ME, MN, MO, NC, NY, OH, OK, PA, RI, SD, TN, TX, UT, VT, WI, and WV.

⁴ The 19 states where Amazon collects sales tax are: AZ, CA, CT, GA, IN, KS, KY, MA, ND, NJ, NV, NY, PA, TN, TX, VA, WA, WI, WV. Amazon has also reached an agreement to start collecting taxes in FL, MD, and SC over the next two years.

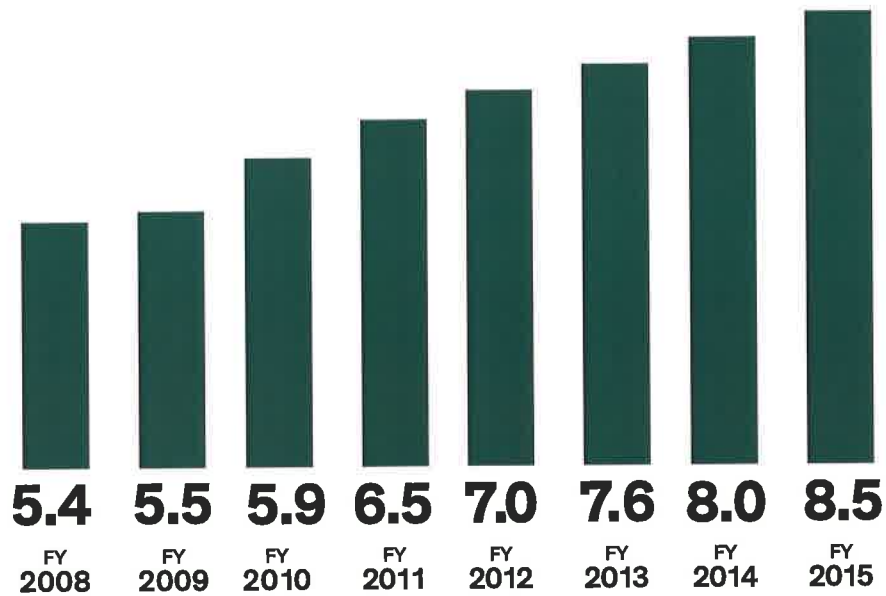
⁵ Public Sector Consultants, “Individual States Moving Rapidly toward Internet Sales Tax Collection An Addendum to Michigan Sales Tax Collection and the Internet: A Need for Fairness,” May 2012.

As of Jan. 1, 2014, Amazon collects sales taxes from ~~50%~~ 60% of customers.



Michigan Retail Sales Lost to Remote Sellers

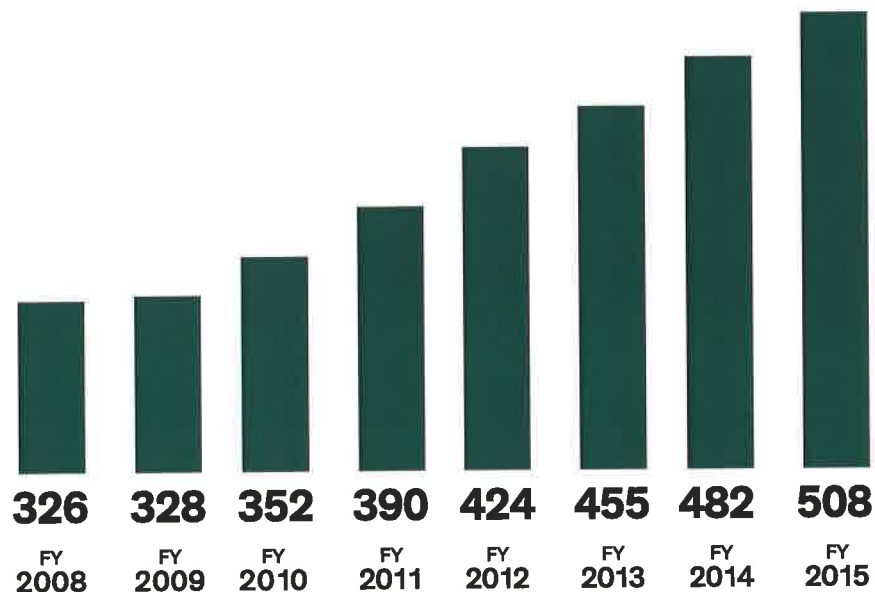
In Billions of Dollars



Source: Michigan Retailers Association from Michigan Department of Treasury Data.

Michigan Consumer Remote Sales and Use Tax Loss Impact

In Millions of Dollars



Source: U.S. Census Bureau. Compiled by the Office of Revenue and Tax Analysis, Michigan Department of Treasury.

Purchasers Use Tax Return

Issued under Public Act 94 of 1937. Filing is mandatory.

The Michigan Use Tax Act, Sec. 3(1) (MCL 205.93), states in part that there is levied upon and there shall be collected from **every person in this state a specific tax for the privilege of using, storing, or consuming tangible personal property in this state at a rate equal to 6% of the price of the property.**

As stated in Sec. 2(f) (MCL 205.92), "purchase price" or "price" means the total amount of consideration paid by the consumer to the seller, including cash, credit, property, and services, for which tangible personal property or services are sold, leased, or rented, valued in money, whether received in money or otherwise, and applies to the measure subject to use tax. "Tangible personal property" is defined in Sec. 2(k) to mean "personal property that can be seen, weighed, measured, felt, or touched or that is in any other manner perceptible to the senses and includes electricity, water, gas, steam, and prewritten computer software."

Purchase price includes "delivery charges," defined in Sec. 2b (e) (MCL 205.92b) to mean "charges by the seller for preparation and delivery to a location designated by the purchaser of tangible personal property. Delivery charges include, but are not limited to, transportation, shipping, handling, crating, and packing."

Therefore, when you purchase items from out-of-state sellers through the Internet, catalogs, newspapers, television or magazines, you may owe use tax. Some out-of-state sellers collect the Michigan tax on sales; when they do, you should pay the tax directly to the seller and disregard this method of payment.

If the out-of-state seller doesn't collect Michigan sales or use tax, you must pay Michigan 6% use tax due directly to the Michigan Department of Treasury on the purchase price as defined above.

Examples of tangible personal property subject to use tax are clothing, electronics, furniture, jewelry or books. Examples of tangible personal property not subject to tax are grocery food items, prescription drugs, vitamins, newspapers and periodicals. An itemized list of purchases is not required.

Please be advised that tangible personal property purchased while traveling abroad or from another state and brought into Michigan for storage, use or consumption is subject to 6% Michigan use tax. However, credit is given for any sales or use tax that had been legally due and paid in another state of the United States up to 6% at the time of acquisition of the property.

Michigan Department of Treasury also provides a use tax line on the Michigan Individual Income Tax Return to report and pay use tax. Report and pay the use tax using this form or the use tax line on the MI-1040, NOT BOTH.

To ensure proper credit please PRINT the following.

Your Name or Company Name		Social Security or Federal ID Number	
Street Address, City, State and Zip		Telephone Number	
Total Purchases (including delivery charges) \$ _____		I declare under penalty of perjury that this return is true and complete to the best of my knowledge. MCL 205.108	
X 6%			
Total Tax Due	\$ _____	Signature	Date

This return is due the 20th day of the calendar month for the preceding calendar month. Make payment payable to "State of Michigan" and write "Use Tax" in the memo area of the check or money order.

Mail this return and payment to the Michigan Department of Treasury, P.O. Box 30781, Lansing, MI 48909

***Make a copy of this return and payment for your records.**